November 19, 1963.

Brief to the Ontario Committee on Taxation

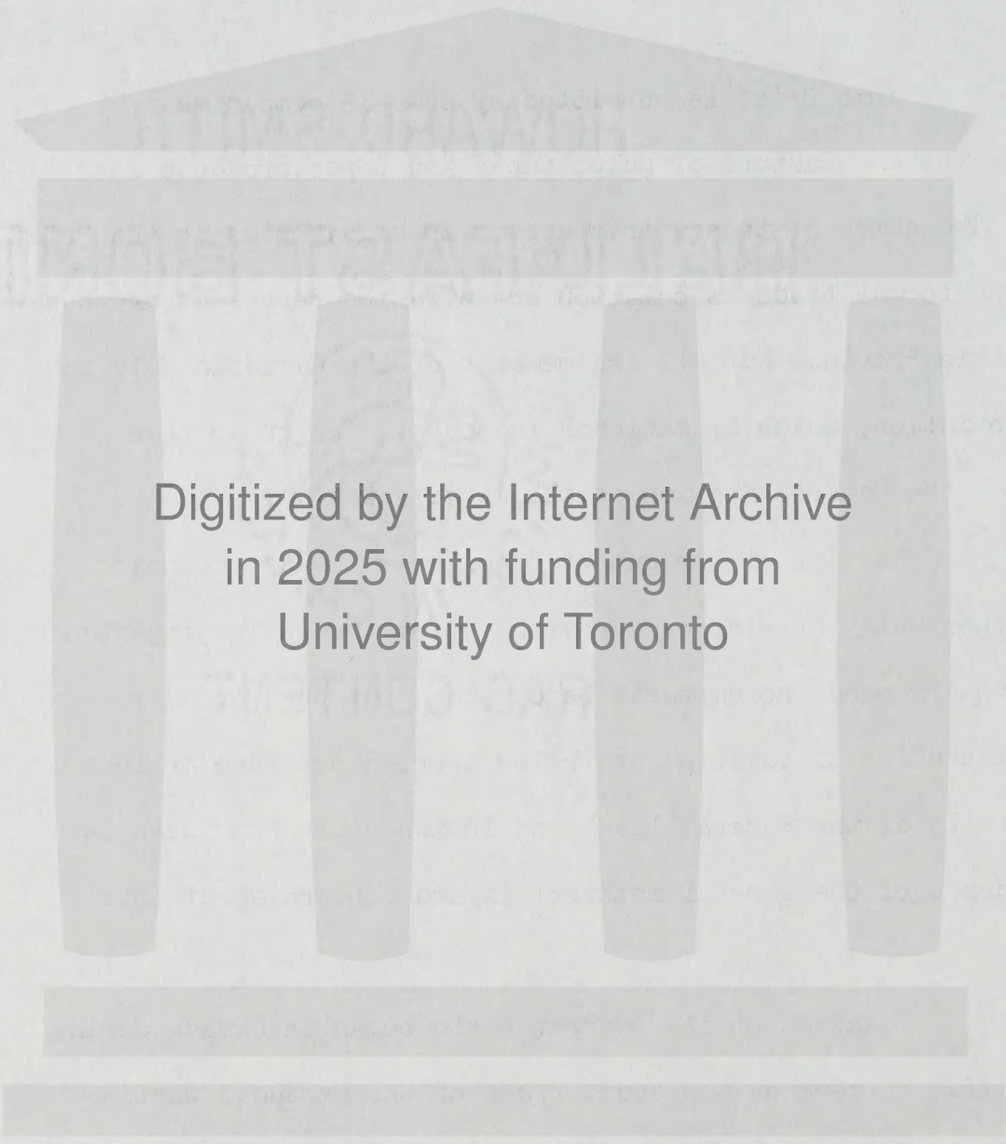
Submitted by the Ontario Pulp and Paper Companies

This Brief is submitted by some 16 companies engaged in the manufacture of pulp, paper and paper products in Ontario. The names of these firms appear as signatories to the Brief. There is no formal trade association organization representing these firms in this Province but all are members of the Canadian Pulp and Paper Association, which is national in scope. The group thus constitutes the Ontario Section of the Association.

We wish at the outset to express our appreciation for the opportunity of placing our views before you. The importance of your enquiry needs no emphasis here: the fact that broadly comparable studies of taxation are being carried out more or less coincidentally at the Federal level and in two other Provinces is ample evidence of the general interest in and concern about this subject.

Taxation on its present scale began in Canada during World War II. It came as the counterpart of the expanded wartime role of government, and in the circumstances of the time was accepted as a matter of necessity. High level taxation continued into the post-war years, as governments and their agencies played an important part in the major job of reorganizing and readjusting the economy to a peace-time basis.

In more recent years, however, new economic circumstances have emerged. For industry in Canada, and for Canadians



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generally, these new circumstances have brought a less vigorous growth environment, intense competition and persistent problems of unemployment. It is against this background, we submit, that fundamental questions must be asked as to the economic effects of taxation on our Provincial - and national - growth and development.

It is not our intention to suggest that government activity should revert to the level which prevailed in an earlier time. The march of events in technology and industrial organization have rendered older concepts of laissez-faire obsolete in today's economic environment. No one, looking around at the ample evidence of our general material well-being, can conclude that the lines of development along which our economic system has evolved, and in which the role of government has been prominent, have been fundamentally wrong.

The appropriate basis of debate is one of degree and not of kind but the need for critical examination and debate is not on this account any less important. To say that we have become adjusted to a high level of government activity in our economy is not the same thing as saying that this activity should expand unchecked. It is only prudent to view these matters from the cost, as well as the benefit, side.

Summary

In the Section that follows, an outline of the size and structure of the pulp and paper industry is given with particular emphasis on the world, and North American, trading environment as it has developed in recent years. As the analysis shows, competition in international markets has become increasingly intense and in these circumstances, the industry is acutely conscious of the impact of taxation on its ability to compete.

It is in this context that our general comments on taxation are given in succeeding sections. From an examination of historical trends of government revenues and expenditures, it is

evident that activities in the government sectors - and in particular at the provincial government level - have been expanding relatively rapidly - much faster, for example, than the expansion of economic activity in the Province as measured by the trend of personal income. We see in these trends cause for concern and a need, therefore, for restraint in the future expansion of governmental activities. We recognize, too, the existence of particular problems in the existence of both Federal and provincial levels of government and we suggest that consideration be given to strengthening the machinery for coordinating and planning activities at the two levels.

It is our view that consideration should be given to reducing corporation taxes in Canada. Additionally, we suggest the need for careful attention to the form of taxation and we conclude that, with the importance of both export and import competition in mind, retail sales taxes are preferable to taxes on income from the standpoint of encouraging investment and economic growth.

We have also commented on recent non-resident withholding tax changes. Though this is a matter of Federal responsibility, we believe that these changes run counter to Provincial policies attempting to stimulate employment and economic growth. This is an example of the need for closer coordination in fiscal matters but we would hope also that your Commission will see fit to urge a more considered course on the part of Federal authorities.

Specifically too, we recommend that the Ontario Logging Tax be repealed. The tax does not add to the overall tax burden of the Ontario pulp and paper companies, nor is this warranted. Its net effect isto produce a relatively small transfer of revenues from the Federal to the Ontario governments but, if this is significant, we feel sure it can be accomplished in a much more straightforward way.

Finally, we include a brief note on proposed Provincial and Federal pension plans. These afford another example of expansion in the government sectors. At the present time, it is not possible to judge the cost implications in any precise way but we feel it to be most important to evaluate these proposals with these implications in mind.

SIZE AND STRUCTURE OF THE INDUSTRY

Pulp and paper has long been recognized as one of Canada's largest industries. The place that it occupies in the Canadian economy is most simply illustrated by the following tabulation, prepared by the Association, of the ten leading manufacturing industries in Canada on the basis of selling value of factory shipments. The figures are for 1961, the latest year of record:

Industry	Value of Factory Shipments Thousands of Dollars
Pulp and Paper	$1,634,606
Smelting and Refining	1,462,457 ✕
Petroleum Refining	1,184,176 ✕
Slaughtering and Meat Packing	1,080,913
Motor Vehicles	870,942
Iron and Steel Mills	789,271
Sawmills	550,915 ✕
Industrial Chemicals	476,603
Pasteurizing Plants	411,633
Metal Stamping, Pressing and Coating	389,642

Source: D.B.S.
✕ Gross Value of Production

Among the industries shown, pulp and paper also ranked first in value added by manufacture, salaries and wages, and employment. The Industry is also a leading earner of foreign exchange: in 1962, its exports amounted to roughly $1,175 millions, equivalent to about 70% of its total output and to some 19% of total exports of Canadian domestic products.

The pulp and paper companies in Ontario constitute an important part of the national industry and of the Provincial economy. In regard to its position in the Canadian pulp and paper

industry, the Dominion Bureau of Statistics reports 125 mills in Canada, of which 39 are located in Ontario; in terms of shipments and employment, the Ontario industry compares as follows:

Pulp and Paper Industry Comparisons, Ontario Versus All Canada

	Ontario	Canada	% Ontario
Value of all Shipments (1962) - 000$	$507,128	$1,675,000(e)	30.3%
Value of Exports (1962) - 000$	$295,656	$1,174,145	25.2%
Employees (1961)	19,985	65,799	30.4%
Salaries and Wages (1961) - 000$	$107,789	$ 355,071	30.4%

(e) Estimated by C.P.P.A. The Ontario Value of Shipments and Exports figures were derived from a special survey of the Firms participating in this Submission.

In general, the Ontario industry makes up roughly one-third of the national industry. The slightly lower proportion in the case of exports indicates that, in relation to the rest of the pulp and paper industry, the Ontario firms distribute a somewhat higher proportion of their output to the domestic market than externally. Essentially, this difference in structure stems from two factors. One of these is the locational disadvantages of Ontario mills in relation to mills in Quebec or Eastern Canada and the West Coast insofar as overseas exports of newsprint and wood-pulp are concerned. Secondly, Ontario is the largest regional market in Canada for fine papers and paperboard and this had led to some specialization on the part of the Ontario mills to serve this market.

Despite these structural differences, the Ontario industry is nevertheless heavily dependent on exports, and particularly exports to the United States. A survey of the distribution of shipments by the Ontario firms in 1962 revealed the following breakdown:

Ontario Pulp and Paper Shipments 1962

Shipments to	Thousands of Dollars	% of Total
Domestic Market	$211,472	41.7%
United States	279,004	55.0
Other Markets	16,652	3.3
Total	$507,128	100.0%

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	Ontario	Canada	% Ontario
Value of all Shipments (1962) - 000$	$507,129	$1,675,000(e)	30.3%
Value of Exports (1962) - 000$	$265,654	$1,174,145	25.2%
Employees (1961)	40,086	65,790	30.4%
Salaries and Wages (1961) - 000$	$107,783	$ 355,071	30.4%

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Out of total shipments of just over one-half billion dollars, the United States market alone absorbed some $279 millions or roughly 55%. The domestic market, valued at over $200 millions in 1962, is obviously also a major source of demand for the industry's output and, beyond this, is of basic importance to the continued growth of the industry, particularly with respect to higher-grade papers and paper products. But it is not an exaggeration to say that, historically, the industry has required access to the large-scale U.S. demand for the great staple products - newsprint and woodpulp - to provide the base from which diversified growth could take place. In this sense, the U.S. market is if anything even more important to the industry's development than the statistics alone would suggest. Exports to other markets, conversely, have played a much smaller part, reflecting the locational considerations referred to earlier.

Industry Taxation

In this outline of the size and structure of the industry in Ontario, mention should also be made of the level of its tax burden. Based on a survey of the 16 Firms participating in this Submission, payments to all levels of governments in the 1962 Fiscal year were as follows:

Taxation of the Ontario Pulp and Paper Industry

		Thousands of Dollars
Federal:	Income Tax	$36,226 (1)
Provincial:	Corporation Tax	$ 7,789 (1)
	Logging Tax	2,811
	Other Provincial Taxes	581 (e)
	Crown Dues, Fire Protection Charges, Land Tax, etc.	6,899
	Sub-total Provincial	$18,080
Municipal Taxes		5,734
	Total All Governments	$60,040

(1) After credit for Ontario Logging Tax
(e) Estimated

In the aggregate, the 16 responding firms paid just over $60 millions to the Federal, Ontario and Ontario municipal governments in 1962. This is equivalent to approximately 12% of the value of factory shipments of the firms surveyed. From the standpoint of the industry's competitive position it will be evident that, at a rate of roughly 12¢ out of the sales dollar, aggregate payments to all levels of governments have become a major factor in the cost of doing business for this industry.

Within the total payments, some $18 millions went to the Provincial treasury, of which $10.6 millions was in corporation and logging taxes. In its reporting of financial statistics of Provincial governments for the fiscal year ending March 1963, DBS shows an estimated $185,010,000 as Ontario Government revenues from corporation income taxes (including, it is believed, the Provincial Logging Tax) levied on all industries. On this basis, the corporation plus logging taxes of the Ontario pulp and paper firms evidently alone accounted for just under 6% of Provincial tax revenues from all corporations in Ontario.

The Industry in a World Setting

As has been noted, woodpulp and newsprint are the mainstays of the industry in Canada; in only slightly lesser degree, this is also true of the Ontario industry. To a considerable extent the industry in Canada has been built on the fact that these commodities move freely in world trade: in 1962, some 92% of Canadian newsprint shipments and 90% of the woodpulp not used by the producing companies themselves went to export markets. The Canadian industry today would be very much smaller, perhaps less diversified and probably less efficient had it been unable to achieve large-scale operations through exports.

The growth of Canadian output of the two major products reflects in large measure the growth of the U.S. market. Around the turn of the Century, developing markets for paper and paper products in that country led to a concern as to the adequacy

of domestic forest resources. U.S. manufacturers extended their operations to Canada, first as a source of pulpwood, then woodpulp. A shift to newsprint production in Canada came after 1911 when this product was permitted duty-free entry into the U.S.

The primary attraction which Canada possessed was its abundance of wood but this was coupled with its wealth in water resources - as a means of transportation, as a process material and as a source of energy - and its generally favourable attitude toward foreign investment. The benefits to Canada were no less considerable: capital and markets, both on a scale far beyond what Canadians themselves could provide.

By 1950, U.S. newsprint consumption had grown to just over 5.9 million tons; the Canadian industry supplied 80% of these needs. In regard to woodpulp, the United States has always been much more self-sufficient. Total domestic consumption of woodpulp in 1950 was 16.5 million tons while imports amounted to roughly 2.4 million tons. But of this tonnage, some 1.7 million tons, or about 70% came from Canada. In turn, an indication of the relative size of the U.S. market in 1950 is given by the fact that it accounted for about 61% of world newsprint demand and close to 45% of world woodpulp demand.

It is not surprising that the United States should have occupied this dominant position in the world pulp and paper picture. The level of consumption of these products usually mirrors the level of economic development generally and in this respect, too, the U.S. led the world. But it will also be recalled that in the year we have been speaking of, 1950, the European countries were still struggling with massive problems of reconstruction and the underdeveloped countries had yet to show signs of significant advance. In part the predominance of the United States in world pulp and paper markets was a reflection of depressed economic circumstances elsewhere.

Woodpulp Trends

Since 1950, the world pulp and paper situation has gradually been changing. Looking first at world woodpulp developments from the demand (or consumption) side, the trends since 1950 can be summarized as follows:

World Woodpulp Consumption

	1950 (000 tons)	1961 (000 tons)	% Increase
Canada	6,663	9,026	35.5%
United States	17,138	27,812	62.3
Western Europe	8,652	18,390	112.6
Other Free Countries	1,732	7,151	312.9
Free World	34,185	62,379	82.5%
Communist Countries	3,833	6,792	77.2
World Total	38,018	69,171	81.9%

Source: United States Pulp Producers' Association. Data are for "New Supply", i.e. production less exports plus imports, which is equivalent to demand in the countries or areas shown.

The relatively slower growth rates in the two markets which are of prime importance to Canada - the domestic and U.S. markets - are obvious.

As we noted earlier, exports of woodpulp have played an important part in the historical development of the Canadian industry; it is relevant therefore to note the growth of these exports in relation to the consumption increases given above. Canadian exports to the Communist Countries, if any, are negligible and these countries are omitted from the tabulation.

Canadian Exports of Woodpulp

	1950 (000 tons)	1961 (000 tons)	% Increase
Exported to			
United States	1,694	2,177	28.5%
Western Europe	129	399	209.3
Other Countries	22	293	1,231.8
Total Exports	1,845	2,869	55.5%

Between 1950 and 1961, Free World demand for woodpulp, excluding domestic demand in Canada, rose from just over 27.5 million tons to approximately 53.4 million tons, or by 94%. Canadian pulp exports to these markets in the period rose by only some 55.5%.

In particular, the increase of 28.5% in our exports to the U.S. has been well below the increase of 62.3% in over-all consumption of woodpulp in that market. U.S. domestic pulp production has increased very substantially in recent years, as the following tabulation shows:

U.S. Woodpulp Consumption

	1950 (000 tons)	1961 (000 tons)	% Increase
Production	14,849	26,523	78.6%
Imports	2,385	2,467	3.4
Exports	-96	-1,178	1,127.0
Total Net Consumption	17,138	27,812	62.3%

This transformation in the U.S. pulp situation has come about in part because of technological changes which have greatly stimulated the production of sulphate pulps in the U.S. South and West Coast. In part, too, it also reflects the fact of relatively low wood costs in the dense and fast-growing forests of these areas. It might be noted in passing that these same considerations have been favourable to pulp operations on the West Coast in Canada: since 1950, production in British Columbia has increased by some 227%.

The breakdown of Canadian woodpulp exports in 1950 and 1961 given earlier above does show very sharp gains in shipments to countries other than the United States, though it is only in recent years that the tonnages have become substantial. These areas show the greatest promise for the future and this development is of course to be welcomed. As was mentioned earlier, however, the Ontario pulp mills are not well situated to serve these markets.

The consequence of the foregoing developments can be illustrated by the following summary of woodpulp production in the 1950-61 period:

World Woodpulp Production

	1950 (000 tons)	1961 (000 tons)	% Increase
Canada	8,473	11,833	39.7%
United States	14,849	26,523	78.6
Western Europe	9,637	18,002	86.8
Other Free Countries	1,255	6,351	406.1
Free World	34,214	62,709	83.3%
Communist Countries	3,646	7,015	92.4
World Total	37,860	69,724	84.2%

Against an expansion in world production (and demand, as shown earlier) of about 84% between 1950 and 1961, Canadian pulp production recorded an increase of only 40%. As a result, Canada's share of production fell from roughly 22% to 17% of the world total.

Newsprint Trends

World newsprint markets present a broadly similar picture. The trend of demand since 1950 in the principal markets or market areas has been as follows:

World Newsprint Consumption

	1950 (000 tons)	1962 (000 tons)	% Increase
Canada	354.6	510.0	43.8%
United States	5,921.4	7,500.0	26.7
Western Europe	1,901.3	4,284.0	125.3
Other Free World	1,020.8	2,772.5	171.6
Free World	9,198.1	15,066.5	63.8
Communist Countries	516.2	1,055.0	104.4
World Total	9,714.3	16,121.5	66.0%

It is quite apparent that the most vigorous growth in newsprint demand has been outside North America. The U.S. market in particular, by far the major outlet for Canadian newsprint, has shown only modest growth.

In this same period, world newsprint production figures have been as follows:

World Newsprint Production

	1950 (000 tons)	1962 (000 tons)	% Increase
Canada	5,278.6	6,710.0	27.1%
United States	1,014.7	2,155.0	112.4
Western Europe	2,537.5	4,428.0	74.5
Other Free World	237.6	1,592.3	570.2
	9,068.4	14,885.3	64.1%
Communist Countries	506.0	1,125.0	122.3
World Total	9,574.4	16,010.3	67.2%

In 1962, Canada was still the leading producer but her predominance has declined sharply. The most striking expansion in production has occurred in the so-called "Other Free World" countries where output increased almost sixfold in the period. This group now lists some 16 countries - in South America, Africa, Australia and the East; in 1950 there were only 8 such countries.

More importantly, however, it will be seen that production in the U.S. has shown a marked increase. The rapid growth of the U.S. newsprint industry occurred almost entirely in the short period between 1953 and 1959: at the beginning of this period capacity was rated at 1,161,000 tons while by the latter year it had reached 2,416,000 tons. Most of this expansion took place in the U.S. South and could be attributed to several factors: the development of Southern pine and hardwood as suitable raw materials, special tax assistance measures instituted by the U.S. government, closeness to market and other advantageous cost factors. For the Canadian industry, the result has been a decline in market share in the U.S. from 80% in 1950 to 69% in 1962.

The Ontario Industry

In general, the experience of the Ontario pulp and paper industry has paralleled that of the national industry. Because it has been less favourably situated with respect to overseas markets, the Ontario industry has been more dependent on the North American market and thus has felt the full effect of

developments in the United States. Data comparing the Canadian and Ontario industry expansion in the 1950-61 period are as follows:

Increases in Production, 1950 to 1961,
Ontario versus the Rest of Canada

	Percentage Increase	
	Ontario	Rest of Canada
Gross Value of Factory Shipments	61.1%	76.0%
Woodpulp for Sale	10.4	80.9
Newsprint	59.9	59.6
Other Paper Grades	97.1	105.3

Figures are in dollar terms and reflect price as well as volume increases in the period.

In regard to newsprint and other paper grades, production in Ontario has increased closely in line with the national trend. The Provincial industry has not fared as well in the production of woodpulp for sale where the larger increase in the national figure reflects the very rapid expansion of production in British Columbia as was noted earlier.

The Future Outlook

In Canada, after the war and on into the boom years of the early 1950's, the view was frequently expressed that we had a unique position in the world pulp and paper industry. The extent of our forest resources and the fact that we had a well-developed industry already trading in world markets gave us, it was felt, a preferred position in relation to the growth in world requirements which could be foreseen.

The industry cannot look forward with the same feeling of assurance today. Historically, as we have seen, the Canadian industry has been closely linked with the U.S. market but this market, with respect to newsprint, is expanding slowly. Moreover, for both woodpulp and newsprint, the United States itself has acquired a growing production capability, based on the use of Southern forest resources which would not have been technically feasible 15 years ago.

Other world markets have experienced strong growth trends in recent years but these trends have been matched by expanding production in the overseas countries. Here again, technological developments have played a leading part, greatly expanding the range of fibrous materials which can be economically converted into pulp and paper products.

Looking ahead, it should not be inferred from these developments that the expansion of the industry in Canada must hereafter be paced by the growth of the domestic market alone. In many instances the rapid expansion of production in other countries has taken place from a very small base, so that the early increases could hardly fail to seem impressive. Frequently, local supplies of raw materials, capable of supporting only limited production, have already largely been taken up. On the demand side, we have noted that world pulp needs rose from some 38 million tons to over 69 million tons between 1950 and 1961, or at a growth rate of nearly 6% per year. The consumption of the bulk of this tonnage occurs in a handful of countries in North America and Western Europe. But with advancing industrialization, rising living standards and increased literacy in prospect for the less highly developed countries, there is reason to expect this growth rate, or a rate close to it, to continue. Canada has the resources to participate in this growth.

The Canadian industry, and perhaps even more so the industry in Ontario, however, now find themselves in a highly competitive situation - and this situation, too, can be expected to continue. The rate of growth which our domestic industry can achieve does not of course turn on the question of its tax burden alone but, at present levels of taxation, it has become a factor of consequence in ultimately determining our ability to compete.

GENERAL COMMENTS ON TAXATION

It is against this industry background that we wish to comment on the level and trends of taxation generally. In greater or lesser degree the competitive pressures that the pulp and paper industry in Ontario is experiencing are being met by other industries: these pressures have become a normal part of the new economic circumstances, referred to at the outset, in which Canadian industry may now expect to operate. In these circumstances, we submit, there is cause for apprehension about the growing financial needs of government.

A check over the past ten years reveals that net general expenditures of the Provincial government have risen from some $372 millions to almost $1,175 millions, thus roughly tripling in the period. Expressed as a growth rate, this increase is equivalent to about 12% per annum. In this same period, Personal Income in the Province increased by only 82%, or at a compound rate equivalent to just over 6% annually.

The trends are of course similar on the governmental revenue side. Looking at the shorter period from 1956 to the present, the period in which problems of employment and growth have emerged with full force, the increase in revenues has continued to be dramatic. The figures are summarized below.

Ontario, Provincial and Municipal Revenues,
Less Subsidies, 1956 and 1962, in Millions of Dollars

	1956	1962	% Increase
Provincial Net General Revenue	$481.8	$1,061.0	120%
Less Federal Subsidies	3.6	4.6	
	$478.2	$1,056.4	121%
Municipal Gross Current Revenue	500.5	884.1	77
Less Federal and Provincial Subsidies	76.4	154.9	
	$424.1	$ 729.2	72%
Total Provincial and Municipal Revenues, excluding Subsidies	902.3	1,785.6	98%

Source: D.B.S. Provincial figures are for year ending March 31, 1957 and 1963. Municipal figures are on a calendar year basis.

The data cover current revenues from all sources, including Provincial revenues under Tax Rental Agreements though, as the Table notes, excluding subsidy payments. In the comparatively short period of six years, current revenues received by the Provincial government have more than doubled. Municipal revenues have been rising at a slower rate but, taken together, the revenues of these two levels of government in 1962 were almost twice as high as in 1956.

A broadly similar though more modest pattern of increase is to be seen in the Federal revenues derived from Ontario sources. These are estimated to have risen from $1,250 millions to $1,727 millions in the 1955/56 - 1960/61 period. A portion of these amounts was returned to the Province under the Tax Rental Agreements and these amounts were included in the Provincial revenue data given earlier. Net of these payments, Federal revenues from Ontario increased from $1,112 millions in 1955/56 to $1,613 millions in 1960/61 a gain of some 45%.

These increases pertain only to current revenues: Federal, Provincial and Municipal borrowings have also risen substantially in this period:

Provincial and Municipal Borrowing Trends, 1956-63
in Millions of Dollars

	1956	1962	% Increase
Ontario Provincial Funded Debt:			
Direct	$ 1,010.6	$ 1,687.8	67%
Indirect	1,110.7	1,601.3	44
	$ 2,121.3	$ 3,289.1	55%
Ontario Municipalities:			
Outstanding Debt	$ 935.5	$ 1,852.2	98%
Federal Debt:			
Direct	$14,442	$17,817	23%
Guaranteed	793	1,631	106
	$15,235	$19,448	28%

Provincial - As at March 31, 1957 and March 31, 1963
Municipalities
and Federal - As at December 30, 1956 and December 30, 1962

The Committee will of course be familiar with the data we have given and no doubt will have available a much more comprehensive analysis than it has been possible for us to undertake. In the summary form in which we have cited them, however, the figures serve to emphasize the relative growth of government revenues and expenditures and to point up the question as to whether these trends can continue. With our open economy the question is an urgent one.

The pressures on governments to increase expenditures are constant: the demand for government services is seemingly endless. For a private industry, the level of demand is determined by the forces of competition, either from other domestic industries or competitors abroad. These competitive forces operate to keep rising costs in check: when costs rise too quickly relative to competitors' costs the industry's sales will be curbed and its expansion will cease.

There is no similar mechanism to regulate directly the expansion of government operations. A mechanism exists but it works much more slowly and indirectly. The rising cost of government must ultimately be met by the private sector of the economy: they become a part of the structure of costs in that sector and it is there that the mechanism of competition is encountered.

It will be true in general terms that rising government costs - rising taxation - will affect all industry equally. Insofar as the domestic economy is concerned, taxation does not discriminate against particular industries or place certain industries at a competitive disadvantage relative to others. Indeed, in a completely closed economy the consequences of high taxation are to be found in the allocation of resources as between the private and public sectors rather than in the relative rates of growth of industries within the private sector.

But we do not have a closed economy in Ontario or in Canada. The level and growth of our economic activity has always required that our industries be in a position to compete on world markets and compete in our domestic markets against foreign suppliers. Here tax costs can affect our competitive position. The danger in the trends of revenue and expenditure noted earlier is that, in increasing the tax burden on our industries we weaken their competitive position. The consequence of this is to limit their expansion.

This is the view, we submit, that must be taken of the rising government revenue and expenditure trends. Canadians have heard much in recent years of 'living beyond their means'. The level of our exports has been too low and that of our imports too high, and we have had a balance of payments problem. We suggest that there is a connection between this problem and the rapid growth in government expenditures at all levels. Perhaps it is in this latter respect that we have been living beyond our means.

International Tax Considerations

We recognize that government expenditures have been rising in other countries. There is cause for concern, however, in the possibility of our governmental expenditures rising more rapidly than those of other countries, or other countries adopting forms of taxation that do not affect so greatly the business cost structure. In this context, President Kennedy's tax proposals which are currently before the United States Senate are of great importance. As you know, these proposals contemplate, among many other things, the reduction of the corporation income tax in two stages down to a top rate of 48% by January 1, 1965. If these proposals are enacted, and if our top rate of corporate income tax is not decreased from its present level of 52% (in Ontario), our industry will be subject to one more cost disadvantage as against its competitors in the United States, its principal market area.

Indeed, we would suggest that our industry, along with other industries in Canada, could not support our present tax rates in the face of a reduction of rates in the United States. This is not to say that our tax structure must precisely emulate theirs or that our tax rates, in effect, must be set externally. But it must be recognized that with international trade such an important part of Canadian economic activity and with, in particular, the close links between the two economies, our tax costs must be 'competitive' or, put another way, cannot be allowed to get out of line. In the final analysis, the ability of our industries to pay taxes is dependent on their productivity. There is no reason to suppose that the productivity of Canadian industry exceeds that of U.S. industry.

With our dependence on foreign trade, we cannot stress too strongly the importance of tax cost considerations. We believe that this must be recognized by all levels of government in Canada. We recognize that the problem of control of government expenditure and taxation is particularly difficult under our Federal system of divided responsibility. If, for example, the Federal government should reduce the rate of corporation income tax its action could be effectively nullified by a compensating rise in the rates imposed by the provinces. Indeed, the particularly rapid growth in Provincial revenue requirements suggests the possibility.

The mere existence of such a possibility may act as a subtle deterrent in any consideration of the possibilities of tax reduction. There is no pat solution to this problem. There must obviously be restraint on the part of both levels of government, and we would hope your Committee will urge the need for such restraint upon the Ontario government. In a practical way, something could probably be done if there were greater communication between the Federal and Provincial governments, by

way of joint study groups or inter-governmental committees, with particular reference to planning and coordinating future activities. We would be surprised if some duplication of effort does not exist as between, say, the Federal departments of agriculture, health, forestry, trade and commerce, on the one hand, and Provincial departments occupying similar spheres on the other.

One minor example of duplication that is visible to the ordinary taxpayer lies in the existence of separate administrations for the collection of corporation income tax by the Federal and Ontario governments and the requirement that separate tax returns be filed for each jurisdiction. We see no substantial reason why the Ontario income tax could not be collected on its behalf by the Federal tax department, as is done for other provinces. While it would then become uneconomic to collect the corporation capital and place of business taxes, this revenue loss would be so minor that it undoubtedly would be recovered in the reduction of administration costs. The taxpayer, for his part, would appreciate having one less form to fill out.

Changes in the Form of Taxation

It is our view that, more than merely holding tax rates in check, consideration should be given to reducing corporation taxes in Canada, as is being contemplated in the United States. Even in the absence of the tax reductions, however, there may be room for adjustment in the form of taxation that will be helpful to the Provincial economy. To illustrate this, suppose that an increase in taxation were under consideration and a choice existed between an increase in the corporation income tax and the retail sales tax. To a purely domestic industry with little import competition, there would be little to choose in the long run. For such industry, the rise in the income tax rate would sooner or later be reflected in its price structure and ultimately the end price to the consumer would rise. A rise in the retail sales tax

would probably be reflected more quickly but otherwise the effect would be the same. On the other hand, to the export industry, or to the domestic industry with serious import competition, the effect might be quite different. Competition from manufacturers outside the country might make a rise in the ultimate selling price impossible. An increase in the income tax rate would then serve only to lower the return on investment in such industry, thereby inhibiting its growth potential. By contrast, a sales tax increase would not affect export sales (in the absence of counter moves by other countries) nor would it disturb the competitive position of domestic manufacturers as against foreign manufacturers. If, then, it is desirable to stimulate investment in Ontario and in Canada, as it would seem to be in the light of recent conditions of slow growth and high unemployment, it would seem wise to emphasize the tax on retail sales as a way of taxing business activity, rather than the tax on income.

Withholding Tax on Interest and Dividends Remitted to Non-Residents

Reference to the need to stimulate investment raises the question of the treatment of foreign capital invested in Canada. From the pure taxation standpoint, this is principally a Federal matter. However, Federal government policy in recent years in some ways runs counter to efforts by the Ontario government and others to stimulate investment, employment and growth in Canada and therefore is of legitimate concern to the province.

The Federal government policy of attempting to discourage foreign ownership of industry in Canada may be questioned on grounds both of fairness and of economic wisdom. For many years the withholding tax rate on dividends to non-residents was 5% where the Canadian company was wholly-owned by a foreign corporation. The fairness of the sudden rise from 5% to 15% at December 20, 1960 may be questioned, as may the measures in the 1963 Income Tax Amending Act raising the rate

to 20% unless there is outside participation of at least a quarter of the voting stock. The earlier pattern was well suited to a country needing to import developmental capital and deriving know-how and other intangible benefits from a parent corporation well established elsewhere. Many subsidiaries of foreign companies were established in Canada under this encouragement and, while such provisions should not perhaps have been expected to be permanent, the suddenness and the degree of reversal of policy, allied with the difficulties of achieving the lower 10% rate provided in the 1963 amending Act, raise the question of inequity to past investors.

The economic wisdom of these measures in relation to future as well as past investment may also be questioned. The future growth of Canada, and also of the pulp and paper industry as a whole and in Ontario, will require large amounts of capital. The fact that Canadian sources of capital remain inadequate to supply this need, as they have been in the past, was graphically illustrated by the temporary panic last summer when the United States administration proposed to place a tax of up to 15% on purchases by Americans from non-residents of foreign (including Canadian) securities.

The pulp and paper industry in Ontario is vitally interested in the free international flow of capital so that it may finance its expansion plans at the lowest competitive cost and so that it may expand, without retaliatory penalty, its marketing activities abroad to assure outlets for its production. The attempt to lessen the degree of foreign ownership in Canada by discouraging investment by non-residents and by encouraging increased Canadian participation in existing investment would inhibit the flow of capital from abroad and would deplete Canadian capital resources, to the detriment of growth. In our view, a much sounder objective would be to

encourage Canadian participation in new developments without discouraging, through withholding taxes, the foreign capital that will be required for a long time to come.

The Ontario Logging Tax

We wish now to turn briefly to two matters of interest specifically to the pulp and paper industry. The first of these refers to the Ontario Logging Tax. Ontario is one of three provinces (Quebec and British Columbia being the others) that imposes a tax on logging profits. Credit is allowed against Federal income tax for the lesser of two-thirds of the amount of the tax or 6-2/3% of the taxpayer's income from logging, while credit is allowed against Ontario income tax for one-third of the tax. As a result, at present rates, there is no overall increase in total tax payments because of this tax.

This peculiar characteristic of the Logging Tax underlines the fact that there is no recognizable rationale for it. It cannot reasonably be regarded as a substitute for a royalty in the use of Crown resources, since it would then be an illogical duplication of Crown dues and stumpage charges. Also, it is imposed on profits from logging private lands as well as Crown lands. It cannot be regarded as a special tax imposed by the province in a field of taxation where it has a prior right since the Federal government should logically then exempt logging income completely from tax, not merely grant a partial tax credit. It cannot even be regarded as a tax especially aimed at the forest industries, since as presently constituted, it does not in the end increase their total tax burden.

The tax was first imposed by Ontario effective in 1949. Initially, the effect of the Logging Tax was to reduce slightly the combined tax liability of the forest industry as compared with other industries in the province. Later, because of changes in Federal-Provincial tax sharing arrangements, the tax resulted in a net addition to the forest industries' total

tax burden. Quite recently, further amendments to the tax statutes produced the present situation where the entire Logging Tax is offset by credits against Federal and Ontario income taxes. It is submitted that there never was a justification for a differential in the tax burden between the forest industry and others, as is now implicitly recognized. We suggest that this should be acknowledged by repeal of the Ontario Logging Tax. We recognize that this would have the result of increasing Federal tax revenues through elimination of the Logging Tax Credit, and correspondingly reducing the Ontario tax revenues. The amount involved, however, is relatively small but, in any case, we feel this to be an inappropriate mechanism to effect a transfer of revenues between governments.

Pension Legislation

We should like also to express to the Committee the concern of this industry over the present confusion surrounding pension legislation at both the Provincial and Federal levels of government. Although we cannot have as yet a full understanding of the implications of the current legislative proposals, we, as an industry largely dependent on export markets, must be particularly conscious of our costs as compared with the costs in other countries.

Most companies in the pulp and paper industry, in common with other large employers in the province, have already established pension plans which were designed to provide reasonable retirement benefits to their employees. Many of these plans are financed entirely by the employers, with no employee contributions being required. Employers in such instances can expect pension costs to increase substantially because of the portability and earlier vesting requirements of the Ontario portable pension legislation.

The proposed Canada Pension Plan will reportedly add what amounts to a tax of close to one percent of a company's payroll. Furthermore, although we are unable to predict accurately the timing or extent, this percentage is expected to increase substantially in the future.

In more general terms, these pension plans represent still another extension of government activity and thus are an example of the pattern of expansion in this sector that was discussed earlier. We suggest therefore that this is an area which should receive the most careful thought and analysis before any decision as to further action is taken.

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In conclusion, we trust we have conveyed to the Commission the extreme importance of taxation as it affects our ability to compete. First, as an industry, we are heavily dependent on export markets, particularly in the United States. Second, the natural advantages that the industry once held over competitors in other countries have diminished, particularly in the last decade. Third, payments to government form a substantial element (about 12%) of our revenues. Fourth, government expenditures at all levels are showing a persistent rising trend, not only in absolute terms but also as a percentage of income. For all of these reasons, the possibility of further increases in taxation and, thus additions to our costs, is a matter of very real concern to the pulp and paper industry in this Province.

All of which is respectfully submitted,

Abitibi Power & Paper Company, Limited
The Beaver Wood Fibre Company Limited
Canadian International Paper Company
Continental Can Company of Canada Limited
Dominion Tar & Chemical Company Limited
Dryden Paper Company Limited
The E.B. Eddy Company
The Great Lakes Paper Company Limited
Interlake Tissue Mills Company Limited
The K.V.P. Company Limited
Kimberly-Clark Pulp and Paper Company Limited
Kimberly-Clark Canada Limited
Marathon Corporation of Canada Limited
The Ontario-Minnesota Pulp and Paper Company Limited
The Ontario Paper Company Limited
Spruce Falls Power and Paper Company, Limited